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Cengage Surfaces

After nine months, Cengage Learning emerges from bankruptcy -- and gets right back to addressing familiar challenges.

By [Carl Straumsheim](#) // April 2, 2014

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CENGAGE LEARNING

[Michael Hansen, CEO of Cengage](#)

Cengage Learning emerged from bankruptcy on Tuesday, returning to the textbook market with less debt and more funding, but also with the same challenges facing the academic publishing industry.

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minating \$4 billion of the debt, and secured an additional \$1.75 billion in exit funding. That plan received final approval from a New York bankruptcy court in mid-March, clearing the way for Cengage to [leave bankruptcy \(http://news.cengage.com/corporate/cengage-learning-emerges-from-chapter-11-completes-financial-restructuring-2/\)](http://news.cengage.com/corporate/cengage-learning-emerges-from-chapter-11-completes-financial-restructuring-2/) after nine months.

According to its five-year [operating plan \(http://www.cengage.com/investor/pdf/2013.07.02_Exhibit_A-Blowout_Materials.pdf\)](http://www.cengage.com/investor/pdf/2013.07.02_Exhibit_A-Blowout_Materials.pdf), Cengage still expects to report shrinking revenue through the 2015 fiscal year. The company aims to identify about \$100 million in cuts through the 2016 fiscal year, half of which will come through reductions in staff.

Looking back in an interview with *Inside Higher Ed* at what he called an “extraordinary case of a Chapter 11 bankruptcy,” Michael Hansen, CEO of Cengage Learning, called Tuesday’s announcement a milestone, but “a milestone only in the sense that the work we’re doing to reposition and reorient the company is only beginning.”

“As much as I like having shaved off \$4 billion of debt, it’s a one-time event, and frankly, it’s not going to guarantee our success any which way,” Hansen said. “We are cognizant of the fact that we have only traveled a part of that journey.”

The company is not the only publisher that has had to reassess the way it conducts its business. Cengage Learning, John Wiley & Sons, Macmillan Higher Education, McGraw-Hill Education and Pearson -- the five major publishers that control about half of the textbook market -- have all been forced to reorganize in recent years as print book sales have dwindled. But instead of a clean transition to digital academic materials, the market has fragmented, with many students opting for less expensive rentals and used print books.

Cengage’s bankruptcy proceedings therefore involved not only negotiating how to address billions of dollars of debt and thousands of copyrights, but also changing the company culture, Hansen said. “I would characterize it as a growing awareness in all positions of the organization that the model that used to make Cengage successful ... is no longer in place,” he said.

The reorganized Cengage “is much closer to a software company than a traditional publisher,” Hansen said. Product development is now handled by five different silos -- jointly led by a general manager and a chief technology officer -- each focusing on related academic disciplines (for example, one silo deals with disciplines that value quantitative skills; another, vocational training, he said).

Such a structure reflects Cengage’s and other publishers’ predictions about the transition from print to digital. Cengage aims to almost double its share of active digital users to 4.8 million by the 2018 fiscal year, according to the operating plan. By that point, 40 percent of the company’s adjusted earnings before interest, taxes, depreciation and amortization will come from digital offerings such as MindTap, a cloud-based learning platform that combines readings and multimedia with assessments and analytics.

investment community in mind) that you are a software company and not a publishing company, but companies of any kind take their shape from the paying customers they try to reach.”

Even with the addition of software tools and platforms, Esposito said, the publishers are still investing in and selling content to the same customers.

“The really interesting change in higher ed publishing in recent years (where Cengage has been a leader) is in the migration from selling books to students through faculty adoptions to selling on the institutional level,” Esposito wrote. “That’s a big thing, and it doesn’t get enough airplay. You don’t have to be a software company to do that.”

‘A Transitory Phenomenon’

“The one thing that we are expecting in the near term is that we are seeing a continued decline of new print textbook sales,” Hansen said. “We will see this decline ... driven not by students not opting for digital solutions, but driven by students opting for rental and, to some extent, used books.”

According to data from the Parthenon Group, three-quarters of students renting textbooks in 2012 would have previously bought a used book. Companies such as Chegg have pounced on that opportunity, as have a number of startups rushing create what has often been referred to as the “Netflix” or “Redbox of textbooks.”

[Packback \(http://www.packbackbooks.com/\)](http://www.packbackbooks.com/), one such startup, last Friday enjoyed a prime-time appearance on ABC’s “Shark Tank.” Its founders also [participated in a Reddit “Ask Me Anything” session \(http://www.reddit.com/r/IAmA/comments/21jxku/i_went_on_shark_tank_accidentally_counteroffered/\)](http://www.reddit.com/r/IAmA/comments/21jxku/i_went_on_shark_tank_accidentally_counteroffered/), where they described Packback’s mission as “fixing the broken textbook industry.” Without hours, the founders of [Texts.com \(http://www.texts.com/\)](http://www.texts.com/) had [created their own session \(http://www.reddit.com/r/IAmA/comments/21ldbi/we_founded_textscm_and_are_also_trying_to_fix/\)](http://www.reddit.com/r/IAmA/comments/21ldbi/we_founded_textscm_and_are_also_trying_to_fix/), saying they “are ALSO trying to fix the broken textbook industry.”

The growth of the rental market is troubling for an industry that has long based success on sell-throughs. Yet in Cengage’s operating plan, under the header “Go-Forward Expectation,” the company is banking on three words: “Rental growth slows.”

“The turn really comes when we as an industry and we as Cengage have developed compelling alternatives to the textbook experience,” Hansen said. “The real inflection point in this market is when a student buys a digital solution that can become a digital substitute for the textbook.”

The first generation of those substitutes is already available, Hansen said, but in their current state, they are “primarily homework solutions.” Future versions will focus on helping students with time management skills and

push textbooks.”

The rental market, meanwhile, doesn’t “present a lot of value” to Cengage, Hansen said.

“These are guys that are trying to innovate around the distribution models for the textbook market,” Hansen said. “In my mind, it is a phenomenon that we have to recognize, but it will be a transitory phenomenon -- frankly, a market that should fall by the wayside if we do our job the right way.”

The company is instead watching startups that deal in analytics and contextual learning with “great interest,” Hansen said. “I am a big believer in that you never buy yourself out of trouble, so I wouldn’t want to see acquisitions as the main feature of our strategy... Obviously now that we have emerged, we have the balance sheet to support acquisitions.”

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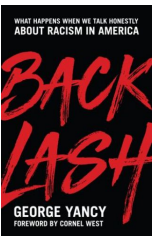
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